

**ABA 203: INTERMEDIATE ACCOUNTING I**

**Instruction to candidates:**

*Answer question ONE and any other TWO questions*

**QUESTION ONE**

M & I Bank Limited has its head office situated on “the hill” to the South West downtown Nairobi. The piece of land of which the building is situated is freehold. The land cost Sh.10 million on 1 July 1989. The building on this piece of land was erected at a cost of Sh.100 million and was completed in June 1991. M & I Bank Limited moved its head office into the building during June 1991, and occupied the whole building. The board of directors estimated that the useful life of the building was 50 years with effect from 1 July 1991. They estimated that the residual value of the building was nil. They decided to have depreciation charged on the straight – line method.

On 1 July 2000 M & I Bank Limited purchased the leasehold of a plot of land in downtown Nairobi. The lease cost of Sh.102 million was for a period of 51 years. Between 1 July 2000 and 30 June 2001, a building was erected on this land at a cost of Sh.300 million. Initially it was planned that a branch of the bank would be situated in the building but this was thought inappropriate. As result, it was decided that the whole building was to be rented out. The estimated useful life of this building was also 50 years and the residual value nil. M & I Bank Limited have found it difficult to find tenants to occupy the building. Income and expenses in relation to this building are as follows (these figures are in the ledger but are not yet reflected in the financial statements):

<b>Year ended 30 June</b>	<b>2002</b>	<b>2003</b>
	<b>Sh million</b>	<b>Sh million</b>
Rental income receivable	24	54
Direct operating expenses including	<input type="text"/>	<input type="text"/>

repairs and	(6)	(12)
Maintenance for floors rented out		
Direct operating expensed including	(6)	(5)
repairs and maintenance for empty	<u>(12)</u>	<u>(17)</u>
floors	<u>(12)</u>	<u>37</u>
Total direct operating expenses		
Net income from investment property		

M & I Bank limited has always used the benchmark treatment for owner occupied under IAS 16 (property, plant and equipment) and the cost model for investment properties under IAS 40 (investment properties) however the directors were concerned about the fair values of the head office building and land the buildings in downtown Nairobi, in case any impertinent losses needed to be provided for under IAS 36 (impairment assets) in the year ended 30 June 2002. As at 30 June 2002, the fair value of the head office land was Sh.50 million and the fair value of the head office building was Sh.468 million – there was no change in the estimated useful life. The fair value of the building in downtown Nairobi at 30 June 2002 was Sh.310 million. Kysons, registered valuers and estate agents carried out this valuation. The directors had Kysons repeat the valuation of the building in downtown Nairobi in June 2003. The fair value at 30 June 2003 will be Sh.318 million.

The directors decide to change the accounting policies in relation to owner-occupied property and investment property, from the benchmark treatment and the cost model to the allowed alternative treatment and the fair value model, respectively. They decide that an adjustment should be made to the opening balance of the retained earnings for the earliest period presented in the accounts to 30 June 2003. The depreciation charge of the year ended 30 June 2002 will not change for the head office building. The directors think that the new accounting policies will result in a more appropriate presentation of events in the financial

statements. The statement of changes in equity should reflect the fact that some of the revaluation surplus is realized as the asset is used by the enterprise.

**Required:**

(a). Show the necessary journal entries required to finalize the accounts for the year ending 30 June 2003, taking into account the changes in the accounting policies. Show the prior period adjustments separately.

(7 marks)

(b). Show extracts from the balance sheet giving the figures as at 30 June 2002 and 30 June 2003 for land, buildings, revaluation reserve and deferred taxation. The rate of tax on income is 30% and on capital gains is nil.

(8 marks)

(c). Show extracts from the income statement that must be disclosed to ensure that the disclosure requirements of the International Financial Reporting Standards are complied with.

**QUESTION TWO**

Mr. Omondi has five acres of farmland. He grows rice sine the area is prone to lots of flooding. He grows rice on four acres and the balance of the area has Mango trees. Other particulars about his farming activities during the year 2009-2010 are:

Opening stock of fertilizers	30,000
Rice saplings purchased	50,000
Water charges	12,000
Sprinkler system	60,000
Pump	30,000
Fertilizer purchases	90,000

Insecticides spraying charges	9,000
Wooden boxes purchased during the year	6000
Jute bags purchased during the year	48,000
Agriculture labour wages	60,000
Orchard labour wages	24,000
Threshing machine	10,000
Dead trees sold	5,000
Salary to Mr. Wanjala (Manager)	6,000

During the year he obtained 90,000 mangoes from his trees, which he disposed off at kshs.10 per dosen. All the boxes were used for packing.

He also obtained 100 quintals rice per acre, half of which fetched him shs.7 per kg and the rest shs.5 per kilo. One tenth quantity of bags purchased remained unutilized. Fertilizers worth shs.20, 000 remained in the stock at the end of the year. Depreciation is to be provided at 10%.Rural development authority of Nyanza region monitors his performance and he need s to provide product wise profit and loss account to them. He apportions common expenses in proportion to area under each product. Insecticides are required to be sprayed once in every three years on mangoes trees to keep them from harmful insects.

You are required to prepare the product wise profit and loss account.

### **QUESTION THREE**

Kaka mega steel ltd. obtained a lease form Kitui Coal ltd. for a coal mine on 1<sup>st</sup> January 2009 on the following terms and conditions

- 1) Royalty at shs, 1 per ton raised

- 2) Minimum rent shs. 24,000 per annum
- 3) Recoupment of short workings of each year during three years following subject to a maximum of shs. 5000 per annum.
- 4) In the event of a strike the minimum rent would be taken pro rata on the basis of actual working days but in the event of lockout, the lessee would enjoy a concession in respect of the minimum rent for 50% of the period of the lockout.

Besides the above, The Kaka mega Steel ltd. have been granted a cash subsidy equal to 25% of the unrecoverable short workings by the Central government up to the first five years of the lease.

Workings up to the first six years are as follows:

2009 Actual royalty	14,000
2010 Actual royalty	20,400
2011 Actual royalty	32,200
2012 Actual royalty	27,200
2013 Actual royalty	21,600 (strike 2 months)
2014 Actual royalty	19,400 (lockout for 4 months)

Show the ledger accounts in the books of the Kaka mega Steel ltd.

#### **QUESTION FOUR**

The following are the particulars relating to a hire purchase

Purchaser ---Wambua and co

Seller -----Omtata and Co

Date of purchase January 1<sup>st</sup> 2010

Goods purchased -----machines

Cash price shs. 12,894

Payments:--shs.2000 on signing of the agreement and the balance in the three equal annual installments of shs. 4000 due on 31<sup>st</sup> December each year.

Rate of Interest ---5% per annum

Depreciation ---20% on the written down value each year

Make the journal entries and prepare the necessary ledger accounts in the books of the parties and show the machinery in the balance sheet as on 31<sup>st</sup> December 2011.

## **QUESTION FIVE**

Write short notes on the following:

a)

- 1) Shortworkings
- 2) Strike and lockout
- 3) Minimum rent or dead rent
- 4) Pisciculture

b) what are the objectives and characteristics of farm accounting

**END**